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COUNTRY AND REGIONAL EXPERIENCES IN ATTRACTING FOREIGN DIRECT INVESTMENT FOR DEVELOPMENT

Foreign direct investment to the least developed countries and other developing countries outside Africa**

Report by the UNCTAD secretariat

SUMMARY

Contrary to the decline of world foreign-direct-investment flows of past years, flows to all developing countries continued to rise, reaching a high share of 31 per cent in world flows in 1992. The only group of developing countries that did not participate in this growth is the least developed countries. As a result, their importance relative to the developing-country total declined from 1.4 per cent during 1981-1985 to 0.6 per cent in 1992, and to the world total from 0.4 per cent to 0.2 per cent.

South, East and South-East Asia continued to be the largest host developing-country region, accounting for 61 per cent of the developing-country total in 1992. China, in particular, attracted considerable amounts of foreign-direct-investment flows, becoming the largest host develcping country. Inflows to the Asian newly industrialized economies were maintained at a high level, but are undergoing a restructuring in the direction of higher quality foreign direct investment. Foreign-direct-investment inflows to Latin America have also increased since the late 1980s, and their annual average

* E/C.10/1994/1.

** See also "Foreign direct investment in Africa", E/C.10/1994/5.

amounts during 1991-1992 were more than twice as large as those in the first half of the 1980s. The importance of subsidized foreign-direct-investment flows is declining, and the challenge is now to ensure that conventional flows can be maintained at a sufficiently high level to sustain recent growth rates in investment flows. Further progress in economic integration would be helpful in this regard. Prospects are good that the current level of flows to the developing countries as a whole will be maintained, if not improved, during the 1990s.

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INTRODUCTION

1. In its resolution 1993/49, paragraph 8, the Economic and Social Council requested the Secretary-General to submit to the Commission on Transnational Corporations at its twentieth session a report on the flows of foreign direct investment to least developed countries and other developing countries. In response to this request, the Programme on Transnational Corporations prepared the present report, in cooperation with the ECLAC/UNCTAD Joint Unit. Beginning with a review of foreign direct investment in the least developed countries, the report turns to an analysis of current trends and patterns of investment flows to Asia and Latin America and the Caribbean. A separate report on foreign direct investment in Africa (E/C.10/1994/5) is also before the Commission.

I. FOREIGN DIRECT INVESTMENT IN LEAST DEVELOPED COUNTRIES

2. Least developed countries 1/ received very few of the investment flows that rose rapidly in the developing world beginning with the mid-1980s. Their share of foreign-direct-investment inflows to developing countries remained not only very small but declined from an annual average of 2.2 per cent during 1986-1990 to 0.9 per cent in 1991 and 0.6 per cent in 1992. Their share of total foreign direct investment in the world was even smaller: 0.2 per cent in 1992 (table 1). In absolute terms, the roughly $0.3 billion of total inflows to all least developed countries in 1992 was about equivalent to the inflows to Pakistan that year.

3. Factors that have discouraged investment inflows to least developed countries have included, generally speaking, the falling global demand for most of their primary exports, coupled often with high levels of external indebtedness; their persistently small domestic investment and slow economic growth (table 2); their small domestic markets; their poorly developed physical infrastructure, including oftentimes difficult and expensive transport and communication links with the outside world; 2/ and a generally unskilled labour force. In a substantial number of least developed countries, political instability and, in some instances, violence and civil strife have become prohibitive deterrents to foreign direct investment. While a number of least developed countries have embarked upon significant structural reforms and liberalized their foreign-direct-investment regulations, 3/ such measures, though necessary and helpful, have not yet proved sufficient inducements for transnational corporations to increase their investments in the group of least developed countries as a whole. The challenge for these countries to attract investment inflows is all the greater because all countries, developed and developing alike, are competing for a larger share of foreign direct investment.

4. This perception is partly offset by locational and other advantages of a number of least developed countries. Least developed countries in Asia, in particular, are well positioned to capture a share of the substantial investment flows that are concentrated in that region. As a number of former foreign-direct-investment inflow leaders among Asian developing countries are graduating

Table 1. Foreign-direct-investment inflows in least developed countries and developing countries, 1981-1992

	1981-1985 (Annual average)	1986-1990 (Annual average)	1991	1992
Least developed countries				
Total (billions of dollars)	0.2	0.5	0.3	0.3
Share of world total (per cent)	0.4	0.4	0.2	0.2
Share of developing-country total (per cent)	1.4	2.2	0.9	0.6
Developing countries a/				
Total (billions of dollars)	13.1	24.9	39.4	46.8
Share of world total (per cent)	26.3	16.2	24.4	30.8
Total without least developed countries (billions of dollars)	12.9	24.4	39.1	46.5
Africa				
Total (billions of dollars)	1.7	2.9	2.7	3.0
Share of developing-country total (per cent)	12.8	11.4	6.8	6.4
Total without least developed countries (billions of dollars)	1.5	2.4	2.4	2.8
Latin America and the Caribbean				
Total b/ (billions of dollars)	5.8	7.6	14.9	14.5
Share of developing-country total (per cent)	44.7	30.7	37.8	31.0
Total without least developed countries (billions of dollars)	5.8	7.6	14.9	14.5
Middle East				
Total (billions of dollars)	0.4	0.4	0.5	0.3
Share of developing-country total (per cent)	3.4	1.8	1.3	0.5
Total without least developed countries (billions of dollars	0.4	0.4	0.4	0.1

	1981-1985	1986-1990	1991	1992
	(Annual average)			
South, East and South-East Asia				
Total (billions of dollars)	4.9	13.7	20.8	28.3
Share of developing-country total (per cent)	37.7	55.0	52.7	60.6
Total without least developed countries (billions of dollars)	4.9	13.7	20.7	28.3

Source: UNCTAD Programme on Transnational Corporations, based on International Monetary Fund balance-of-payment tape, retrieved on 13 December 1993, data from the UNCTAD Programme on Transnational Corporations foreign-direct-investment database and the OECD secretariat.

a/ Includes developing countries in Europe (Gibraltar, Malta and former Yugoslavia).

b/ The differences in total figures between this table and table 8 are mainly due to the inclusion of Bermuda here. Data for Bermuda for 1992 are not available.

Table 2. Macroeconomic indicators and foreign-direct-investment inflows in developing countries, 1986-1993

(Percentage)

Item	Least developed countries	Developing countries					World
		Total	Africa a/	Latin America	Middle East b/	South, East and South-East Asia	
Growth rate of foreign direct investment							
1986-1990 (average)	.. c/	21.0	7.4	15.7	21.4	35.9	32.6
1991	-52.7	24.3	18.3	73.6	-1.9	4.9	-21.3
1992	-15.3	18.7	12.5	-2.6	-50.0	36.5	-6.0
1993	..	..	..	..	..	..	..
Growth rate of gross domestic product							
1986-1990 (average)	2.1	4.7	2.5	2.0	3.4	7.1	3.6
1991	0.6	4.5	1.6	3.3	2.4	6.1	0.6
1992	0.4	5.8	0.4	2.5	7.8	7.8	1.7
1993 d/	..	6.1	1.6	3.4	3.4	8.7	2.2
Export growth rate e/							
1986-1990 (average)	2.7	11.4	3.7	5.0	7.6	13.1	6.1
1991	0.4	8.1	1.9	4.7	3.1	11.9	2.4
1992	0.1	9.5	2.1	8.5	8.4	11.2	4.6
1993 d/	3.6	9.4	0.1	4.1	6.9	12.7	3.0
Ratio of external debt to gross domestic product							
1986-1990 (average)	68.7	35.3	59.7	48.9	29.8	24.2	..
1991	55.2	32.3	58.9	43.6	24.0	24.9	..
1992	50.5	28.6	56.1	37.3	19.9	23.8	..
1993 d/	48.1	27.2	56.0	37.5	16.8	24.2	..
Gross fixed capital formation as percentage of gross domestic product							
1986-1990 (average)	16.1	24.2	20.9	19.7	21.8	29.3	..
1991	15.1	24.8	20.8	20.8	23.9	29.0	2.0
1992 d/	15.4	25.0	20.9	21.2	23.8	29.3	3.0
1993	..	..	..	..	..	..	..

Source: UNCTAD Programme on Transnational Corporations, based on International Monetary Fund, balance-of-payments tape, retrieved on 13 December 1993, and data from the OECD Secretariat; International Monetary Fund, World Economic Outlook (Washington, D.C., IMF, 1992 and 1993); UNCTAD, The Least Developed Countries 1992 Report (United Nations publication, Sales No. E.93.II.D.3).

a/ Egypt and the Libyan Arab Jamahiriya are included in Middle East except for the item on foreign direct investment.

b/ Includes developing countries in Europe (Cyprus, Malta and Turkey) except for the item on foreign direct investment.

c/ Due to negative inflows in 1986, growth rates cannot be calculated. Excluding the 1986 and 1987 data, the average growth rate was 24 per cent.

d/ Projection by the International Monetary Fund.

e/ Volume of merchandise exports. Data for least developed countries are estimated.

to higher value-added activities, some least developed countries in Asia stand to inherit labour-intensive forms of foreign direct investment at the low end of the value-added chain where low-cost labour is a comparative advantage. Bangladesh and perhaps Cambodia fall into this category. In relation to the Caribbean Basin Initiative and its proximity to the North American market, Haiti has the potential to achieve a similar role with respect to foreign direct investment sourcing. Other least developed countries will continue to play an important role as sources of raw materials important to nearby developed and industrializing markets, such as Myanmar with respect to East Asia. Yet other least developed countries have a potential for attracting foreign direct investment in certain niche areas of international demand, such as tourism in the cases of the Maldives, Nepal and the United Republic of Tanzania. In that connection, to the extent that such countries are successful in attracting additional investment inflows through their liberalization of pertinent regulations and effective promotional campaigns, even limited additional inflows could prove substantial, given their small economic base.

5. Among the developing country regions, Africa has the largest concentration of the least developed countries (31 out of 47). They account for 80 to 90 per cent of the total foreign-direct-investment flows to these countries. Changes in flows to the African least developed countries therefore largely determine the behaviour of investment flows to this entire group of countries. Neither the least developed countries as a group nor African least developed countries have participated in the investment boom to developing countries that began in the late 1980s and continues into the 1990s. In the second half of the 1980s, it looked as if these countries could break out from the period of falling foreign direct investment: between 1985 and 1990, flows grew from $209 million to $355 million. 4/ The early 1990s brought, however, a contraction of flows to $254 million in 1991. Flows during the period 1980-1992 never returned to their highest level, reached in 1980, that is, $444 million. 5/ Within the group of African least developed countries, inflows are highly concentrated: five countries absorbed close to or over 90 per cent of the annual inflows in some years (table 3). The table illustrates the rapidly changing fortunes as regards investment inflows: only Botswana and Zambia were consistently on the list of the largest host countries in all years, while the other large host countries during the early 1990s differed from that during the early 1980s. In addition, inflows in 1991 were such that countries leading the list that year would have hardly made it to the list in 1980. However, a number of least developed countries in Africa occasionally receive amounts of foreign direct investment which, though small in absolute size, are very large when related to the size of their host economies. For example, with annual average flows of $31 million in 1991-1992, Equatorial Guinea led the list of the largest host countries in Africa as a whole, ranked by the share of foreign-direct-investment inflows in gross domestic product. 6/ Botswana, also an important host country by both relative and absolute measures, is an example of a country with a relationship with transnational corporations that benefited its long-term economic growth. 7/

Table 3. The five largest host countries among African least developed countries, based on foreign-direct-investment inflows, 1980, 1985, 1990 and 1991

(Millions of dollars)

1980		1985		1990		1991	
Botswana	112	Zaire	69	Zambia	203	Botswana	45
Zaire	110	Botswana	54	Botswana	38	Equatorial Guinea	42
Zambia	62	Zambia	52	Sierra Leone	32	Zambia	34
Niger	49	Togo	17	Madagascar	22	Sierra Leone	30
Togo	42	Rwanda	15	Lesotho	17	Mozambique	23
The share in Africa's least developed-country total a/ (per cent)	85		99		88		68

Source: UNCTAD Programme on Transnational Corporations, based on International Monetary Fund, balance-of-payments tape, retrieved on 13 December 1993.

a/ Excludes Liberia.

6. A number of least developed countries in Africa hardly receive any foreign direct investment at all. But there is also another group in between the non-receivers and the largest host countries. Countries belonging to this group have not attracted recently meaningful amounts of investment, and their flows in the past fluctuated widely between disinvestments in some years and not negligible amounts of flows in other years. But the fact that they are able to attract such amounts, though only for a short period of time, suggests that they are within the purview of foreign investors; the challenge for them is to sustain the attention of foreign investors. The list of these countries, ranked by the highest inflows in any one of the years between 1980 and 1992, is contained in table 4.

Table 4. Highest amounts of foreign direct investment attracted by individual African least developed countries during the period 1980-1992

(Millions of dollars)

Country	Amount	Year
Somalia	64	1987
Mauritania	27	1980
Malawi	25	1987
Lesotho	21	1988
Rwanda	21	1988
United Republic of Tanzania	19	1981
Gambia	15	1989
Benin	13	1991
Burundi	11	1981

Source: UNCTAD Programme on Transnational Corporations, based on International Monetary Fund, balance-of-payments tape, retrieved on 13 December 1993.

7. The least developed countries in Asia seem to be faring better than countries in other regions: their flows increased during the early 1990s, compared to the second half of the 1980s, except for Afghanistan. Among those which have adopted market-oriented economic policies recently, the Lao People's Democratic Republic and Myanmar attracted some investments (table 5). Inflows of foreign direct investment to the Lao People's Democratic Republic between 1989 (when foreign-direct-investment projects started for the first time) and 1992 totalled $27 million. In this country, 102 permits were granted to foreign investors (mostly from Thailand) in 1992 and 79 in the first half of 1993, mainly in services (including banking). 8/ Myanmar is also beginning to attract some investment, as compared from the 1980s when it received virtually none. Major investors are Thailand, the United States, Singapore and Hong Kong. Flows of foreign direct investment to the Solomon Islands and Vanuatu have been the largest. Given the small size of these countries, these flows are very large relative to the size of their economies (table 5).

Table 5. Foreign direct investment and some economic indicators in selected least developed countries in Asia and Latin America and the Caribbean

Least developed countries	Foreign direct investment (Annual average, million dollars) 1981-1985	1986-1990	1991-1992	Per capita foreign direct investment 1991-1992 a/ (Dollars)	Foreign direct investment as percentage of gross domestic product 1991-1992 b/	Per capita gross domestic product 1990 (Dollars)	Per capita gross domestic product growth rate 1989-1990
Afghanistan	0.06	0.08	-0.3 c/	-0.02	-	485	-8.4
Bangladesh	-0.04	2.16	2.55	0.02	0.01	200	3.7
Haiti	6.64	7.44	10.8	1.66	0.44	380	-3.2
Lao People's Democratic Republic	-	2	8.5	2.02	5.4	206	3.3
Maldives	-0.32	4.04	6.55	32.75	0.01	605	11.2
Myanmar d/	0.08	0.7	1.7	0.04	0.1	548	1.8
Nepal	0.12	1.94	3.1	0.16	0.98	159	1.0
Samoa	0.06	1.40	4.1	20.5	2.9	697	-5.7
Solomon Islands	0.9	5.88	15.35	51.17	11.5	446 e/	4.1
Vanuatu	5.78	9.62	15.25	76.25	7.6	999	1.8
Yemen	21.94	8.82	4.4 c/	0.38	0.06	782	..
All least developed countries	181	539	318	0.59	0.19	311	1.5
All developing countries	13 083	24 942	43 105	15.2	1.58	964	0.5

Source: same as in table 1; United Nations Conference on Trade and Development, The Least Developed Countries 1992 Report (United Nations publication, Sales No. E.93.II.D.3), tables 1, 2 and 7, pp. A-3 - A-5 and A-12.

a/ Average foreign-direct-investment flows during 1991-1992 divided by population in 1990.

b/ Average foreign-direct-investment flows during 1991-1992 divided by gross domestic product in 1990.

c/ 1991 only.

d/ On an approval basis, cumulative inflows of foreign direct investment reported by the Government were $1,008 million between the end of 1988 (when the foreign-direct-investment law was promulgated) and 1993; see Nihon Keizai Shimbun, 1 February 1994.

e/ 1989.

8. Manufacturing has become an increasingly important sector of foreign direct investment in a number of Asian least developed countries. Bangladesh leads in this respect in terms of having the highest percentage of total exports being manufacturing exports; i.e., about three quarters of the total. The corresponding foreign direct investment has also been in the manufacturing sector, in particular textile industry (box) Nepal has also received foreign direct investment for the production of manufactures, especially textiles, which with other manufactures, such as rugs, account for nearly two thirds of that country's exports. 9/ Foreign direct investment in Nepal, however, has also concentrated on the tourism industry, with significant multiplier effects for the economy in terms of the sale of locally manufactured products and the provision of other services. The Maldives is a third country that has also received investment in industrial production (which accounts for one third of its exports) and especially for the development of tourist hotels and resorts. 10/ Another country that has received substantial foreign direct investment in industry, especially for the production of toys and sporting goods, has been Haiti, the only least developed country in the Western Hemisphere. Given the inducements of the Caribbean Basin Initiative and the attraction of a low-paid labour force, foreign direct investment has played a substantial role in that country's economy, in which three quarters of all exports are manufactures. 11/

9. The least developed countries, as all other developing countries, are trying to attract foreign direct investment to their economies, seeing in this investment a potential support for development. In doing so, they encounter many difficulties. Most of these difficulties are related to their low level of development. The continuing inflow of official development assistance will be essential to overcome them. However, many of these countries have locational advantages, which, if coupled with political and economic stability and friendly policies towards domestic and foreign companies, can attract some foreign direct investment. These advantages include natural resources, touristic attractions and a low-cost labour force. In addition to overall foreign-direct-investment liberalization measures, which are necessary, although not a sufficient ingredient of a good investment climate, targeting specific industries or even firms interested in matching their interests with the locational advantages of least developed countries might be a possibility that could be explored, apart from general promotional efforts. Transnational corporations from other, middle-income developing countries should not be left out of such efforts: as the following sections will show, they are becoming a source of foreign direct investment to the regions in which they are located.

BOX. Foreign direct investment in Bangladesh

Bangladesh presents an interesting case of a least developed country that has been successful in obtaining a growing share of investment flows. Rising labour costs and skills have led to the graduation of a number of other Asian countries to higher value-added activities. As a result labour-intensive activities are migrating from them to countries like Bangladesh. On an approval basis a stock of foreign direct investment was 871 million taka ($22 million) as of August 1992, not including export-processing zones.a/ Investment flows to Bangladesh amounted to $3.7 million in 1992, up from $1.4 million in 1991.

Foreign investors have been attracted to Bangladesh's manufacturing sector by both the country's low wages and, in particular, because of that country's unused quota for exporting textiles and apparel to the markets of the European Union and the United States. With garment exports rising from virtually nil in the 1970s to 40 per cent of Bangladesh' export earnings by the end of the 1980s, foreign investment in this industry accounted for nearly one fifth of approved investment inflows in 1992, exclusive of export-processing zones. This industry was initiated in 1979 through a collaborative agreement between Desh Garment Company, a local Bangladesh firm, and Daewoo Corporation, a transnational corporation based in the Republic of Korea which provided labour training, start-up assistance and overall supervision of production and marketing. b/

Aside from the textile and apparel industry, foreign direct investment in Bangladesh has been important in the food processing (20 per cent of cumulative approved investment by mid-1992), electric machinery (14 per cent) and chemical (13 per cent) industries. These investments, as with investments in textiles and apparel, tend to be concentrated at the low end of the value-added chain. Investors have been mainly from other Asian developing countries, accounting for more than three quarters of approved investments between mid-1990 and mid-1992. Firms from the Republic of Korea have in particular dominated investment in the export-processing zones, employing three times as many workers as Japanese firms (6,000 workers versus 2,000 workers) and exporting $4.3 million a month in 1992, compared to $2.3 million of exports by Japanese affiliates.c/

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a/ Stock data are not available for foreign direct investment including export-processing zones.

b/ For details, see United Nations, Transnational Corporations and Management Division, World Investment Report 1992: Transnational Corporations as Engines of Growth (United Nations publication, Sales No. E.92.II.A.19), pp. 214-215.

c/ Japan External Trade Organization, JETRO Hakusho: Toshi-hen, 1993 (Tokyo, JETRO, 1993), pp. 234-237.

II. ASIA AND THE PACIFIC

A. Net resource flows

10. Recent increases in long-term net resource flows to developing countries as a whole reflect the slow-down in developed-country economies and better economic performance and prospects in developing countries, and especially in the countries of South, East and South-East Asia, where these flows have been dramatically increasing since the late 1980s. 12/ As a result, this region accounted for 39 per cent of all flows to developing countries in 1992, compared to 33 per cent in 1986. 13/ These increases reflect not only the highest economic growth rates in the world (table 2), but also good access to international capital markets as well as the development of local capital markets. China has become the single largest recipient among developing countries, attracting in 1993 more than one third of resource flows to South, East and South-East Asia and some 15 per cent of flows to all developing countries. Net resource flows to China represent now 6 per cent of its gross national product. 14/

11. Foreign direct investment and portfolio investment have become the largest and most dynamic components of these flows. 15/ For the region as a whole, the share of foreign direct investment in all resource flows increased from 27 per cent during 1986-1990 to 34 per cent in 1992 (table 6); that of portfolio investment rose from 8 per cent to 13 per cent. The significance of these two types of flows varies, however, among subregions. In South Asia, which accounted for only 15 per cent of resource inflows to the region in 1992, official lending and grants are the most important instruments in external financing, accounting, on average, for 51 per cent and 32 per cent, respectively, of the total resource flows during 1986-1992, as this subregion did not attract substantial private flows. In East and South-East Asia, however, private resource flows accounted for 71 per cent of all resource flows in 1992.

12. The rapidly growing foreign-direct-investment and portfolio-investment flows hold much promise for the region, the needs of which for external financing are enormous: it has been estimated that South and South-East Asia alone will need more than $1 trillion to finance infrastructure projects and capital-intensive industries over the next decade. 16/ To satisfy needs of this magnitude the countries of the region are increasingly using international and local capital markets. In the Eurobond market alone, Asian firms (excluding Japanese ones) issued bonds worth $14.7 billion in 1993, more than six times the 1992 volume. 17/ Major issuers were firms from the Republic of Korea. Firms from India, Malaysia, Pakistan and Thailand are also using this market increasingly.

Table 6. South, East and South-East Asia: net resource flows, by type, 1986-1993 a/

(Billions of dollars)

Type of flow	1986-1990 (Annual average)	1991	1992	1993 b/
Foreign direct investment c/	7.5	14.5	21.1	26.1
Portfolio investment	2.2	4.3	8.1	..
Bonds	0.8	3.2	3.4	..
Equity d/	1.3	1.1	4.7	4.5
Loans	12.9	21.1	26.0	..
Official	10.1	12.1	11.0	14.1
Commercial banks e/	1.9	6.4	7.7	..
Other private	0.9	2.5	7.3	..
Grants f/	4.9	5.7	6.7	7.0
Total	27.5	45.5	61.8	72.3

Source: The World Bank, World Debt Tables 1993-94: External Finance for Developing Countries, Volume 1. Analysis and Summary Tables (Washington, D.C., The World Bank, 1993), pp. 178-181.

a/ Excludes short-term flows.

b/ Projection by the World Bank.

c/ Due to the different coverage of countries, the figures are slightly different from those in table 1. For instance, Taiwan Province of China is not included here.

d/ Gross figures.

e/ Includes both publicly guaranteed and non-guaranteed loans.

f/ Excludes technical-cooperation grants.

13. Local capital markets are also expanding rapidly. The stock market in China alone grew from nothing in 1991 to $32 billion in 1993. The market capitalization of the stock markets in the Republic of Korea, Malaysia and Thailand increased significantly: price indexes rose by more than, respectively, four times, two times and six times by the mid-1993 over 1984. 18/ It is evident from the experience of these countries that liberalized access of foreign firms to local capital markets has had a positive impact on the performance of their markets.

B. Foreign direct investment

14. Fuelled by high growth rates, large and increasingly affluent domestic markets, low production costs in a number of countries and a further liberalization of foreign-direct-investment policies, investment inflows in East, South and South-East Asia (including the Pacific) 19/ reached $28 billion in 1992, an increase of 36 per cent over the previous year (table 1). With inflows exceeding $11 billion, China emerged as the largest recipient of foreign direct investment among all developing countries in 1992, and dominated flows into Asia. 20/ Investments increased further to about $26 billion in 1993. 21/ Excluding China, the increase in investment inflows to East, South and South-East Asia was considerably less in 1992: 5 per cent, for a total of $17 billion.

15. Investment inflows in the Republic of Korea and Taiwan Province of China fell by 51 per cent and 31 per cent, respectively, in 1992 (table 7). Investments into Hong Kong and Singapore declined in 1991, then increased by 31 per cent and 28 per cent, respectively, in 1992. The amount of 1992 investment flows into Singapore was only 7 per cent higher than in 1990, and for Hong Kong it was only 40 per cent of the level of the 1990 flows.

16. Despite the decline or slow-down in inflows, the newly industrialized economies as a group attracted almost the same very high level of foreign direct investment in 1992 as during the late 1980s (figure 1), and they continue to rank among the top 10 recipients of this investment among developing countries. This performance may well signal the beginning of a structural change in response to a loss of certain advantages and the acquisition of new ones. Advantages that made these economies attractive to foreign investors in the 1980s - a stable macroeconomic climate, high growth rates of per capita income, expanding consumer markets, export-oriented trade policies, a well-developed (though in some parts crumbling) infrastructure, a highly productive and educated workforce with entrepreneurial capabilities and an indigenous suppliers' network - remain unchanged. Furthermore, Hong Kong and Singapore have the most liberal investment regimes among developing countries, granting, among other things, unrestricted national treatment to foreign investors in all areas.

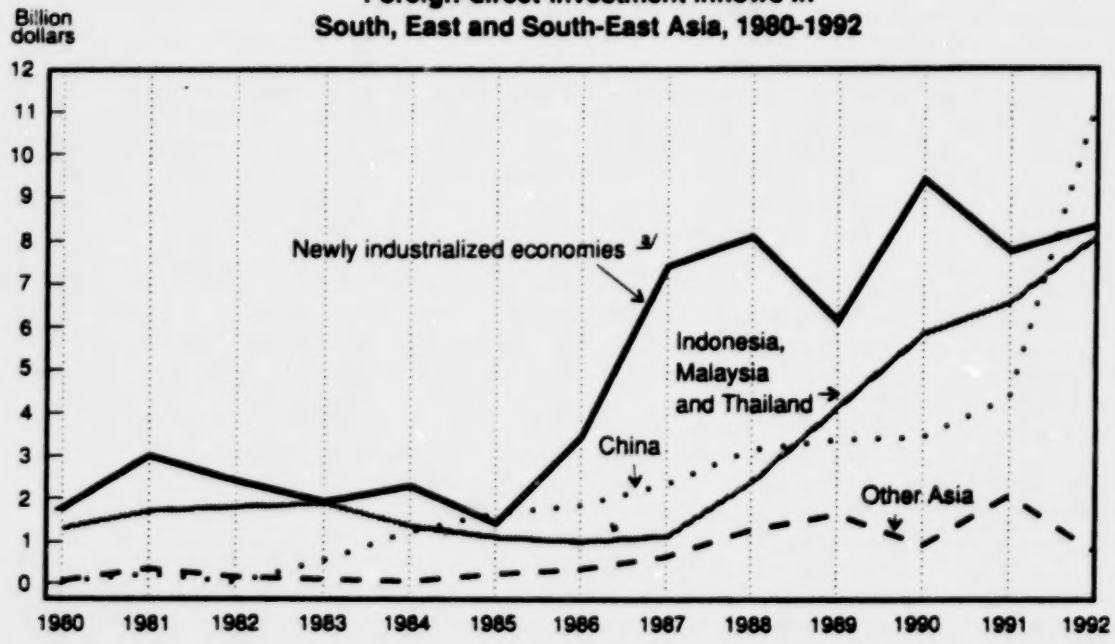
Table 7. Foreign-direct-investment inflows in selected South, East and South-East Asian countries, 1981-1992

(Millions of dollars)

Country	1981-1985 (Annual average)	1986-1990 (Annual average)	1991	1992
China	850	2 853	4 366	11 156
Hong Kong	576	2 034	977	1 272
India	59	167	141	151
Indonesia	236	599	1 462	1 774
Malaysia	1 083	1 123	4 073	4 118
Pakistan	77	175	257	275
Philippines	63	493	544	228
Republic of Korea	112	676	1 116	550
Singapore	1 349	3 247	4 395	5 636
Sri Lanka	42	40	68	123
Taiwan Province of China	189	987	1 271	879
Thailand	279	1 188	2 014	2 116
Viet Nam	6	6	32	24

Source: See table 1.

Figure 1.
Foreign-direct-investment inflows in South, East and South-East Asia, 1980-1992



Source: UNCTAD Programme on Transnational Corporations, based on International Monetary Fund, balance-of-payments tape, retrieved on 13 December 1993, data from the OECD Secretariat and national official sources.

a/ Hong Kong, Republic of Korea, Singapore and Taiwan Province of China.

17. Despite these attractions, it appears that rising costs in excess of productivity gains and an overburdened infrastructure (predominantly urban and road transportation) have discouraged some types of foreign direct investment in these economies in recent years. Real wages increased by 30 per cent in Hong Kong, by 68 per cent in the Republic of Korea and by 36 per cent in Singapore between 1985 and 1990, 22/ while productivity gains during the same period were, for example, only 18 per cent in Singapore and 46 per cent in the Republic of Korea. 23/ The loss of cost advantages of these economies has induced not only foreign, but also domestic companies to shift labour-intensive production abroad and thus expedite the process of industrial upgrading at home. These economies (and, recently, Malaysia) are becoming increasingly interested not so much in the quantity, but rather in the quality of investments and wish to attract high value-adding activities of transnational corporations. 24/ The establishment by transnational corporations of research-and-development facilities or regional headquarters with important coordinating roles fosters an expansion or upgrading in their activities in the host countries that do not necessarily lead to large investment flows.

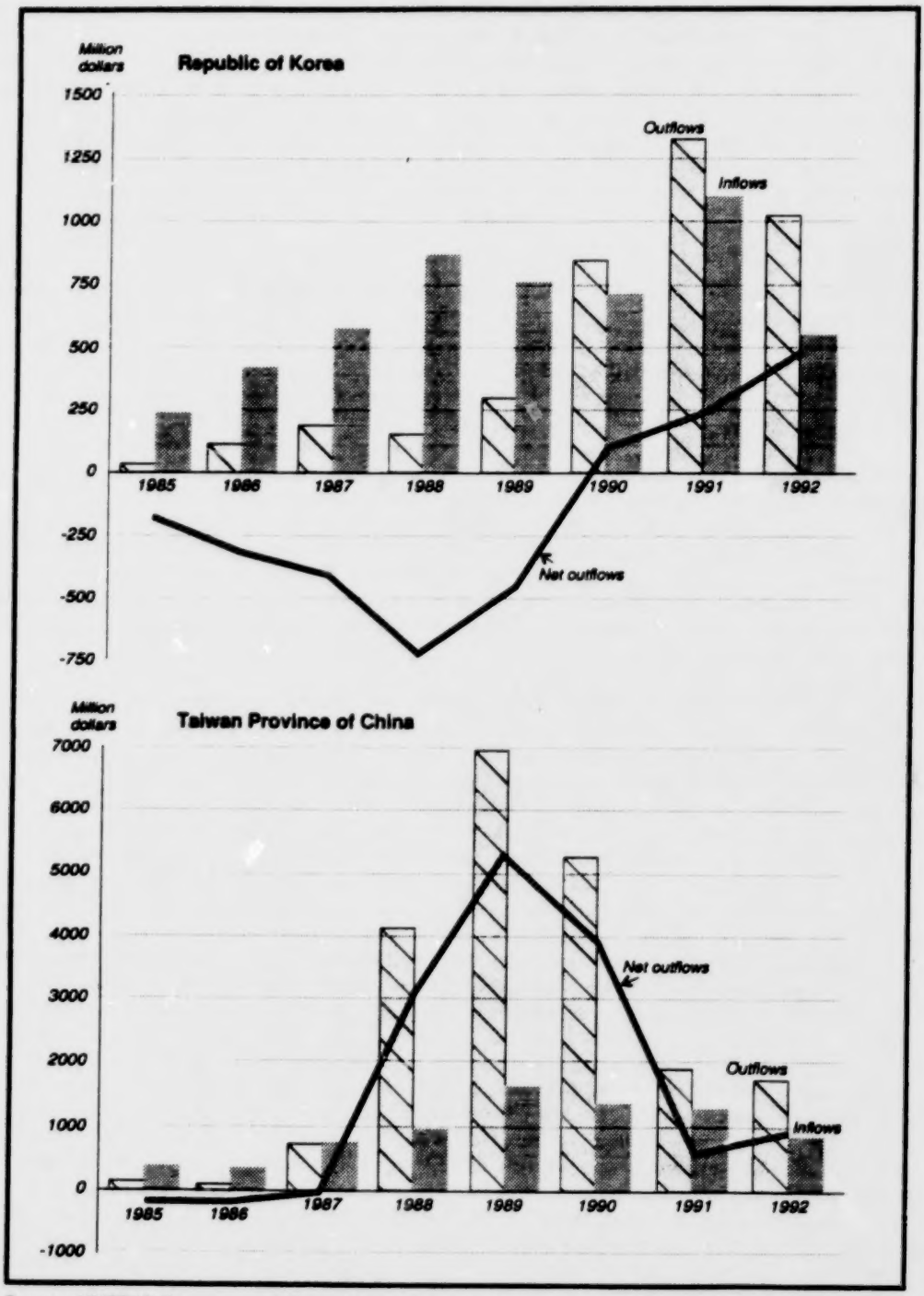
18. As regards outward investment, as part of the restructuring process, firms from the newly industrialized economies continue to invest abroad, in some cases to the extent that they became net foreign investors. For the Republic of Korea and Taiwan Province of China, outflows have exceeded inflows of foreign direct investment, since 1990 for the former and since 1988 for the latter (figure 2). Firms from Singapore, which have been lagging as outward investors compared with those from the other two economies, have recently undertaken a number of investments in China, Malaysia and Indonesia, in an effort to boost their regional presence. 25/ Although most of the foreign direct investment from the newly industrialized economies is located in developing countries of Asia, the share of North America and Western Europe in this investment has recently increased. 26/

19. Investments in Asia are often motivated by rising production costs in home countries. Preferred investment locations have been the member countries of the Association of South East Asian Nations (ASEAN), but in 1993 China and Viet Nam became increasingly attractive. The level of investments in ASEAN countries except Singapore in 1993 reached only 60 per cent of the 1992 level. 27/ Foreign direct investment in developed countries typically seeks to secure market shares and access to technology. 28/ In addition to the newly industrialized economies, China, being the largest host developing country, has also become the largest source of foreign direct investment from developing countries, with investments in both developed and developing countries. 29/

20. The fact that the share of the newly industrialized economies in investment inflows into Asia has diminished in recent years also reflects the emergence of a "second-tier" group of industrializing countries (Indonesia, Malaysia and Thailand) and China, where foreign direct investment grew rapidly in the late 1980s and 1990s, from low initial levels. Those countries became preferred locations for labour-intensive and, more recently, market-seeking foreign direct investment (including by transnational corporations from the newly industrialized economies) as a means both of reducing costs and serving the growing domestic markets. In Thailand, for example, there was only a 3 per cent increase in real wage rates between 1985 and 1991; the real wage level in that country was only 19 per cent of that of the Republic of Korea in 1991.

21. Japanese transnational corporations in particular have invested heavily in those emerging countries at the expense of the newly industrialized economies. Investment outflows into the newly industrialized economies from Japan, their principal source country, declined steadily from 60 per cent to 24 per cent of all investment outflows into South, East and South-East Asia between 1989 and 1992. 30/ Recently, Japanese transnational corporations facing financial difficulties and low profits at home and abroad, as well as an appreciating exchange rate, have been seeking to reduce costs by shifting production to the second-tier industrializing countries and China. In such cost-cutting efforts, wage increases that outstrip productivity gains appear to be an important consideration in the decision of Japanese firms as to where to locate production in Asia, which places the newly industrialized economies at a disadvantage.

Figure 2.
The Republic of Korea and Taiwan Province of China as net foreign direct investors, 1985-1992



Source: UNCTAD Programme on Transnational Corporations, foreign-direct-investment database.

22. An additional incentive to foreign direct investment in the region may come from the decision of the members of ASEAN to deepen economic integration by establishing, in 1993, the ASEAN Free Trade Area with a view to eliminating intra-regional tariffs and non-tariff barriers. Despite the fact that the members of ASEAN have already received considerable amounts of investments from outside the region, if the scheme succeeds in creating a larger economic area, it is quite likely that it will bring about a significant impact on flows of foreign direct investment from both outside and inside the region. The low level of trade interdependence among the ASEAN members - intra-regional trade accounted for only 17 per cent in the members' total trade in 1992 31/ - indicates great potential for the expansion of mutual trade resulting from the elimination of trade barriers.

23. In summary, the decline or slow-down of investment flows into the newly industrialized economies reflects the loss of some advantages, especially in low cost production. These factors are, at least partly, compensated by large and growing domestic economies that offer investment opportunities to market-seeking foreign investors, new investment opportunities in services through the gradual removal of remaining barriers, and policies that encourage quality foreign direct investment that do not always become apparent in inflows. The last of these factors can contribute not only to the upgrading of domestic production structures, but also to the development of new advantages to attract activities of transnational corporations with a high technological content. The loss of foreign direct investment which was a result of traditional advantages need not cause concern if it reflects an economy's movement to a higher developmental stage. For the newly industrialized economies, that loss may have helped to accelerate the process of industrial restructuring by encouraging outward investment by domestic firms.

24. Investment inflows in South Asia increased by 18 per cent in 1992. Since the 1992 statistics do not capture the consequence of the ongoing liberalization of India's investment regime and its success in attracting foreign direct investment, inflows in this region are very likely to increase in 1993. Between August 1991 (when the new industrial policy liberalizing India's investment regime was introduced) and February 1993, more than 2,300 foreign collaborations had been approved in India, with foreign direct investment amounting to Rs 67 billion ($2.6 billion), more than five times the total foreign direct investment approved between 1981 and 1990. 32/ Inflows into other countries in South Asia remain relatively small, hindered in part by the small size of the domestic market, though rapid growth was registered in Pakistan and Sri Lanka (table 7). Viet Nam, which opened to foreign direct investment only in 1988, has also experienced rapid increases in foreign direct investment, especially from other countries within the region. On an approval basis it attracted a total of nearly $7 billion of investment by November 1993. 33/ The recent removal of restrictions to trade and investment by the United States should induce a further spurt of investment in Viet Nam.

25. The Middle East continues to receive small amounts of foreign direct investment (table 1). The attractiveness of that region largely depends on oil deposits. Low and relatively stable prices for petroleum since the latter half of the 1980s have not much encouraged investment inflows. The share of foreign-

direct-investment flows to this region in total flows to developing countries declined to less than 1 per cent in 1992.

III. LATIN AMERICA AND THE CARIBBEAN

26. The Latin American and Caribbean region continues to attract an increasing volume of foreign investment, after a very difficult period during the 1980s when foreign capital inflows virtually dried up and what little arrived was generally obtained only at the cost of substantial incentives. 34/ In particular, during the mid-1980s the region had lost its position as the principal recipient of foreign direct investment among developing countries as it was surpassed by developing Asia. 35/

27. The revival of capital inflows to the region reflects not only the recovery of economic growth after the recession of the 1980s but also the abandonment of the particular import-substitution model 36/ that had been central to the Latin American scheme of industrialization and that had attracted the major part of foreign-direct-investment flows during the previous decades. The structural adjustment programmes carried out by most countries of the region, which encompass major initiatives in respect of market-oriented reforms - especially improvements in governments' fiscal positions - and a new external orientation, especially in terms of a liberalization of production, trade and finance, were showing results during the first years of the 1990s, not only with respect to economic activity in general but also with respect to foreign capital inflows in particular.

A. Net resource flows

28. Total net resource inflows to the region have increased substantially during the present decade, reaching an average annual level of $32 billion during 1991-1992, up from $13 billion during 1986-1990 (table 8). As a result, the region's share of these flows to developing countries rose from 17 to 21 per cent. For the first time since the international debt crisis engulfed the region, the net transfer of resources (subtracting interest payments and other net resource-service expenditures from resource inflows) turned positive in 1991. 37/ This encouraged further the reopening of capital markets for the region. Since the late 1980s, this has been accompanied by significant changes in the composition of resource flows. Before the debt crisis, during the late 1970s and early 1980s, flows to the region consisted mainly of bank credits lent to or guaranteed by Governments, or both. 38/ In the early 1990s, the dominant forms of external finance were non-bank foreign investment, either portfolio (especially equity shares) or direct, aimed at private companies (table 8).

Table 8. Latin America and the Caribbean: net resource flows, by type, 1986-1993 a/

(Billions of dollars)

Type of flow	1986-1990 (Annual average)	1991	1992	1993 b/
Foreign direct investment c/	6.4	12.4	14.5	17.5
Portfolio investment	-0.8	8.9	5.5	..
Bonds	-1.2	2.7	-2.4	..
Equity d/	0.4	6.2	7.9	6.0
International issues	..	4.7	4.0	..
Direct equity	..	0.8	3.6	..
Country funds	..	0.7	0.3	..
Loans	5.4	3.5	7.7	..
Official	5.2	2.4	0.3	3.4
Commercial banks e/	-0.6	2.8	9.7	..
Other private	0.8	-1.7	2.3	..
Grants f/	2.2	4.0	3.1	2.9
Total	13.2	28.8	30.8	37.5

Sources: The World Bank, World Debt Tables 1993-94: External Finance for Developing Countries, Volume 1. Analysis and Summary Tables, op. cit., pp. 186-189, and ECLAC/UNCTAD Joint Unit on Transnational Corporations.

a/ Excludes short-term flows.

b/ Projection by the World Bank.

c/ Due to the different coverage of countries, the figures are slightly different from those in table 1. For instance, Bermuda is not included here.

d/ Gross figures.

e/ Includes both publicly guaranteed and non-guaranteed loans.

f/ Excludes technical-cooperation grants.

29. The major change in the external finances of the region is the emergence of equity portfolio investment as a principal component of these finances. It increased from an annual average of $360 million during 1986-1990 to an average of $7 billion during 1992-1993. As a result, the regions's share in total equity investment flows to the developing world increased from 18 per cent during 1986-1990 to 46 per cent in 1993, while that of South, East and South-East Asia declined from 68 per cent to 36 per cent. Equity portfolio investments encompass several instruments. The most important ones are

international share issues, followed by direct equity purchases and country funds (table 8). Some of them are new. American Depository Receipts (ADRs), for instance, were invented to place new share issues on the United States stock markets. 39/ Argentine, Brazilian, Chilean, Mexican and Venezuelan private companies have been principal users of this instrument. Compared to international and direct share issues, country funds are not that important, measured by value. As a confidence-building factor during the late 1980s, however, they were quite important. 40/

30. The reasons for these changes include earnings differentials between investments in the United States and those in the region, and regained confidence in the security of investments in the region. Reduced gains from portfolio investments due to low real interest rates and sluggish markets (such as the real estate market) in the United States on the one hand, high real interest rates, appreciating currencies and large gains in local stock markets on the other hand led to a relative increase in the attractiveness of Latin American markets. 41/ This was particularly relevant for the new modalities of equity investment. 42/ Other factors include the economic recovery of the region, the international orientation of its companies, as well as liberalization measures that have provided better access to foreign investors and reduced transaction costs.

31. In summary, Latin America and the Caribbean have re-established their access to international capital markets. However, this does not imply a return to the same patterns that preceded the debt crisis. The reopening of capital markets for borrowers from the region rests primarily on access to new and different capital markets. The two principal novelties revolve around greatly increased portfolio investments (especially equity investments) and the revival of foreign-direct-investment flows. For the most part, this new situation relies more on non-bank investors in private sector enterprises than on bank loans to public sector borrowers.

B. Foreign direct investment

32. Foreign-direct-investment inflows to the region expanded in the early 1990s, doubling the annual average of 1986-1990 (tables 1 and 8). The rise in these inflows continued in 1993. As shown earlier, the resurgence of foreign-direct-investment flows to Latin America and the Caribbean was embedded in a broader phenomenon, that is, a substantial increase of private capital flows to the region.

33. One of the most interesting aspects of the increase in foreign-direct-investment flows during the past few years is that it has coincided with a relative decline in the use of exceptional incentive programmes, such as debt-equity conversions and privatizations. 43/ In this sense, a new kind of "normalcy" is reappearing in the region with respect to foreign-direct-investment inflows, viewed from the perspective of the instruments utilized.

34. As table 9 suggests, the new profile of a post-debt-crisis reality is taking shape. Some major debtor countries that undertook harsh adjustment programmes which incorporated heavy incentives, such as debt-equity conversions and privatization programmes, are now enjoying the fruits of stable growth. Among these fruits is the return of conventional (i.e., not heavily subsidized) foreign-direct-investment inflows. Such is the case for both Chile and Mexico. 44/ The new tendency towards normalcy in foreign-direct-investment flows appears to be most pronounced for these two countries.

35. A second category includes some major debtor countries that are still in transition from the foreign-direct-investment subsidization stage of the adjustment process to a sustained recovery stage characterized by more conventional foreign-direct-investment flows. For countries such as Argentina and Venezuela, for example, subsidized foreign direct investment still plays an important role in explaining foreign capital inflows (49 per cent in the case of the former in 1992, and 78 per cent in 1991 with regard to the latter though it declined sharply in 1992), and those inflows have not yet taken on a sustained nature. Fears have been expressed that subsidized foreign direct investment may result only in a change of ownership of existing assets without contributing substantially to the capital formation upon which much future growth depends. 45/

36. A third category includes major debtor countries that have not yet resolved the principal issues related to this indebtedness, that must make further efforts towards macroeconomic stabilization and that have not yet benefited substantially from foreign-direct-investment flows related to privatizations. Countries such as Brazil and Peru are in this category. Recent flows to Brazil, while relatively large in absolute terms, have been small in comparison to the size of the economy and the history of foreign-direct-investment inflows to that country. Brazil, however, may now be on a growth path.

37. Another interesting aspect of the renewed foreign-direct-investment flows to Latin America and the Caribbean is their destination. In terms of countries, it is more than evident that the flows during 1991-1992 for the countries listed in table 9 were increasingly concentrated in Mexico (34 per cent) above and beyond all others. Much further back in respect of volume were countries such as Argentina (22 per cent), Venezuela (9 per cent) and Chile (4 per cent). Announced foreign-direct-investment plans for 1992-1994 were very much concentrated in Mexico and Chile in value terms. 46/

38. The countries that succeeded in attracting considerable foreign-direct-investment flows did so especially in the services and natural resources sectors, sectors in which privatization programmes were concentrated. 47/ About $7 billion (or two thirds) of the foreign direct investment that entered Mexico during 1991-1992 went into services industries (communications, tourism, financial and professional services). 48/ Similarly, $1.1 billion foreign-direct-investment inflows into Argentina and $1.5 billion into Venezuela were in this sector, primarily in the power-generation, telecommunication and transportation industries.

Table 9. Latin America and the Caribbean: foreign-direct-investment inflows, by instrument, 1988-1993

(Millions of dollars)

Country/instrument		1988	1989	1990	1991	1992	1993 a/	1988-1992 total
Argentina	Total	1 147	1 028	1 836	2 439	4 179	3 300	10 629
Conventional foreign direct investment		807	869	-80	1 586	2 112	732	5 294
Debt-equity conversion		340	159	815	-	-	-	1 314
Privatization		-	-	1 101	853 b/	2 067 b/	2 568	4 021
Brazil	Total	2 969	1 267	901	972	1 454	2 000	7 563
Conventional foreign direct investment		882	321	618	850	1 359	..	4 030
Debt-equity conversion		2 087	946	283	68	95	..	3 479
Privatization		-	-	-	54	-	..	54
Chile	Total	1 027	1 505	691	563	737	850	4 523
Conventional foreign direct investment		2	69	249	563	737	850	1 620
Debt-equity conversion		886	1 321	442	-	-	-	2 649
Privatization		139	115	-	-	-	-	254
Colombia	Total	203	576	500	457	790	830	2 526
Conventional foreign direct investment		203	576	500	405	790	..	2 474
Debt-equity conversion		-	-	-	-	-	-	-
Privatization		-	-	-	52	-	..	52
Mexico	Total	2 594	3 037	2 632	4 762	5 366	6 900	18 391
Conventional foreign direct investment		1 671	2 648	2 432	3 956	5 275	..	15 982
Debt-equity conversion		868	389	85	19	-	-	1 361
Privatization		55	-	115	787	91	..	1 048
Peru	Total	26	59	41	-7	127	200	246
Conventional foreign direct investment		26	59	41	-7	-13	..	106
Debt-equity conversion		-	-	-	-	-	-	-
Privatization		-	-	-	-	140	..	140
Venezuela	Total	89	213	451	1 916	629	256	3 298
Conventional foreign direct investment		39	30	148	161	545 a/	256	923
Debt-equity conversion		50	183	303	256	70 a/	-	862
Privatization		-	-	-	1 499	14 a/	-	1 513
Total above	Total	8 055	7 685	7 052	11 102	13 282	14 356	47 176
Conventional foreign direct investment		3 630	4 572	3 908	7 514	10 805	..	30 429
Debt-equity conversion		4 231	2 998	1 928	343	185	..	9 665
Privatization		194	115	1 216	3 245	2 312	..	7 082
Latin America and the Caribbean c/		9 047	6 287	8 585	14 903	14 513	17 508	53 335

Sources: A. Calcagno, "Inversión extranjera directa e integración: la experiencia reciente de América Latina y el Caribe", Industrialización y desarrollo tecnológico (Santiago, CEPAL, 1993) and ECLAC/UNCTAD Joint Unit on Transnational Corporations.

a/ Estimates by ECLAC/UNCTAD Joint Unit on Transnational Corporations.

b/ All debt-equity conversion activities in 1991-1992 were directly related to privatization.

c/ The differences in total inflows between this table and table 8 are mainly due to the inclusion of Bermuda here. Data for Bermuda for 1992-1993 are not available.

39. A second focal point of new foreign-direct-investment flows was natural resources. Here, the petroleum sector has been the largest recipient. The privatization of the State petroleum company, YPF, and State gas companies in Argentina, and the auctioning of petroleum concessions produced the single largest inflow of foreign direct investment during 1991-1992, at about $2 to 3 billion. In Colombia, the new and massive Cusiana fields produced the recent increase in foreign-direct-investment flows there, which is expected to reach $1.6 billion. 49/ Copper and gold mining projects, often in joint ventures with the State copper company, CODELCO, accounted for the single largest portion of new foreign direct investment to Chile (about $1 billion); there is also significant activity in cellulose projects.

40. In the manufacturing sector, which used to be the core of foreign-direct-investment activity in this region during the inward-looking import-substitution period, foreign direct investment was less dynamic, although two major exceptions ought to be noted. The first concerns the adaptation of foreign affiliates already present in the region to the new liberalized and more competitive environment of the local market. Although the overall dimension of the phenomenon is still not clear, foreign direct investment, aimed at restructuring foreign affiliates of transnational corporations that once specialized in supplying solely local markets, with the aim of making them more internationally competitive, is becoming increasingly apparent as transnational corporations alter their international strategies to take into account the impact of trade liberalization in Latin America and the Caribbean. The clearest and most important example of this approach remains that of the automobile industry in Mexico 50/ where new investments in the order of $4 billion have been announced for the 1993-1995 period. Announcements of major investments by automobile manufacturers in Brazil and Argentina in the context of Protocol 21 of the agreement establishing Mercosur suggest that the restructuring of this industry there is beginning to take form. 51/

41. The second major exception to the generally sluggish picture for foreign direct investment in the manufacturing sector in the region during the past few years concerns the maquiladora industry. The surge in foreign direct investment taking advantage of United States legislation that offers tax incentives for the use of export-processing zones for materials originating in the United States has continued. This investment goes not only to border industries in Mexico but to a number of small economies as well (Costa Rica, Dominican Republic and Jamaica). The principal activities involved here include electric and electronic equipment and clothing. Thus, unlike past experiences with foreign direct investment in the manufacturing sector, the new foreign direct investment is mainly characterized by an increasing specialization and an export orientation, as the automobile and maquiladora industries suggest.

42. In sum, foreign-direct-investment flows to Latin America and the Caribbean have strongly increased, with some subsidizing instruments (especially debt-equity swaps) becoming less important to attract such flows. Except for Mexico and perhaps Chile, privatization programmes remain an important tool to attract investment. Flows remain concentrated in a few countries and exhibit certain sectoral characteristics stemming from the particular situations of the principal recipients. Yet they have in common an increased export orientation. Overall, and with the exception of Mexico and to a certain degree Argentina,

manufacturing has, comparatively speaking, attracted less foreign direct investment. Inflows in the primary and tertiary sectors benefited greatly from privatization programmes. Within the basic framework of liberal foreign-direct-investment and trade policies, there may therefore be more scope to attract more investment into the manufacturing sector. Although the specific experiences of Mexico, and to a much lesser extent those of Argentina's privatization programme, have left a significant imprint on the new profile of the region during the 1990s, foreign direct investment is playing an important role in the growing integration of the region into the international economy.

C. Foreign direct investment and integration into the international market

43. The new economic policy in Latin America and the Caribbean clearly rests on the idea that the region's future depends on an improvement of its international competitiveness and its further integration into the world economy, now considered to be beneficial for the countries of the region. The means of this integration include not only trade but also external finance and, in particular, foreign direct investment. Therefore, the liberalization of legislation relating to foreign capital flows has been a prominent aspect of the region's landscape for several years now. 52/ While this perspective is generally shared by virtually all Governments of the region, strategies to attain this objective vary appreciably, especially in respect to the geographical scope of such integration (global, interregional or intraregional), its sequence and speed.

44. The framework for global integration is given by the multilateral trade negotiations within the Uruguay Round. Free trade agreements within the region exemplify intraregional efforts. And agreements with extraregional partners so far focus primarily on Mexico's participation in the North American Free Trade Agreement (NAFTA).

45. With regard to the multilateral trade negotiations, virtually all countries of the region have arrived at the conclusion that an open and unencumbered international trade, investment and financial system is of fundamental importance to their objectives. The region has supported therefore strongly not only the Uruguay Round but also greater trade liberalization in all its forms, especially that leading to increased access to the markets of developed countries. There was a considerable concern in many countries of the region during 1993 when doubts arose in respect to the successful conclusion of the Uruguay Round and United States approval of NAFTA. The best evidence of this new liberal policy is that the region, during the past decade, has embarked on the liberalization of foreign-direct-investment and trade policies, often in a unilateral fashion, coupled with a strong export orientation. In particular, the trade-liberalization programmes of nine principal countries of the region between the mid and late 1980s led to a reduction of average tariffs by half, from 20 to 40 per cent to 10 to 20 per cent; similarly, maximum tariffs and the number of tariff ranges declined steeply. 53/

46. The strengthening of intraregional links (without restricting further integration into the international market) has been based so far mainly on a

grid of bilateral agreements. 54/ Some 33 agreements were concluded during 1985-1993; of these, 27 were approved and 6 have implementation dates falling in the period 1994-1998. The most active countries have been Colombia (9), Venezuela (9), Mexico (8), Chile (7) and Argentina (5). While Colombia and Venezuela have concentrated more on agreements with partners within their Andean Pact integration scheme, Mexico and Chile have agreements with a wide array of partners, including extraregional ones in the case of NAFTA, which Chile expects to join in 1994. As a result of multilateral tariff cuts and these agreements, intraregional exports grew from 10 to 17 per cent of total exports between 1988 and 1992. Furthermore, foreign direct investment grew appreciably, admittedly from a narrow base. Chilean investments in privatized power companies in Argentina were prominent elements of this new regional foreign direct investment.

47. The NAFTA agreement represents so far the only free trade agreement involving extraregional (United States and Canada) partners. 55/ It has also the strongest provisions for the liberalization of foreign direct investment. 56/ Its negotiation provided a strong boost to foreign-direct-investment flows to Mexico during 1986-1992. As a result, that country emerged as the most important recipient of such inflows in Latin America and the Caribbean. Many transnational corporations have now incorporated Mexico into their international production systems. In fact, Mexican companies began to invest in the United States, most notably in the cement and glass industries.

48. Most of the other Latin American countries, fearing that NAFTA could develop into a sort of closed regional grouping with one or at most a few Latin American countries clustered around a North American core, have manifested their interest in becoming party to that agreement. The prominent exceptions have been Brazil 57/ and Cuba. High in the priorities of those wishing to join is the desire to gain improved access to the North American market. However, because foreign direct investment has become the principal means to gain such access as specialized suppliers to that market in the context of new corporate strategies by transnational corporations, the importance of attracting foreign direct investment is critical to obtain the benefits from NAFTA membership.

49. A principal reason why Latin American countries are interested in NAFTA over other integration schemes is that it represents an investment-led integration process, as evidenced by considerable foreign-direct-investment flows that Mexico has obtained. 58/ By comparison, other Latin American integration schemes, which were policy-led, have not generated much in the way of new foreign direct investment. That was most evidently the case of the Andean Pact, dating from 1969, which incorporated a foreign investment code (decision 24) in its original common market format. 59/ It also seems to be the case for the Mercosur (Argentina, Brazil, Paraguay and Uruguay) integration scheme, set to begin as a customs union in 1995. With the exception of foreign direct investment by automotive firms interested in taking advantage of the trade aspects of Protocol 21, little in the way of increased and sustained foreign direct investment has resulted from the Mercosur scheme itself.

50. In summary, the desire to attract foreign direct investment is the key factor behind the interest of Latin American and Caribbean countries in integrating with the North American market. While international liberalization

measures as well as intraregional trade agreements are creating a more competitive environment, they have led so far only to small increases of investment inflows meant to serve international or intraregional markets. As regards the latter, however, trade liberalization has laid the foundation for a restructuring of previously domestic-market-oriented foreign direct investment in the direction of regionally-oriented corporate networks (e.g., the automobile industry in Brazil). Progress towards greater economic regional integration could, therefore, generate and attract greater amounts of foreign direct investment for the regional market and, in this manner, contribute to the economic growth in Latin America and the Caribbean.

IV. CONCLUSIONS

51. Foreign direct investment to developing countries in the aggregate has grown rapidly in recent years, but the flows remain unevenly distributed among developing regions and countries. A number of Asian countries with rapidly growing economies and a well-trained, relatively low-paid labour force have been the main recipients of growing investment flows. In some countries in Latin America, adjustment programmes with debt-equity swap provisions and major privatization elements have accounted for much of the growth of foreign direct investment. For the most part, however, countries, in particular least developed countries, with low growth rates, small markets, unstable economic or political conditions, unresolved debt overhangs, few economically viable public enterprises to privatize and lacking a skilled even if low-paid workforce have seen their foreign-direct-investment levels stagnate at already low levels. The main exceptions to this generalization include those countries where deposits of natural resources are being exploited.

52. Prospects of future foreign-direct-investment flows to the developing countries as a whole are bright, and they provide grounds for guarded optimism with respect to some least developed countries as well. South, East and South-East Asia, as well as Latin America, are expected to experience strong growth in the foreseeable future. There is a strong relationship between the size of and/or changes in gross national product and inflows of foreign direct investment: in the case of South, East and South-East Asia, a one-per-cent increase in gross national product is expected to lead to a 1.6 per cent increase of foreign-direct-investment inflows; in the case of Latin America, that percentage is estimated to be 3.1 per cent. 60/ Furthermore, in Latin America the reduction of indebtedness plays a role in inducing inflows of foreign direct investment: a one-per-cent decrease in indebtedness is estimated to increase investment flows by 0.6 per cent. As the economies in these regions continue to grow and the size of debt is expected to decline, positive effects on flows of foreign direct investment into these regions should materialize.

53. Because of the tendency for key Asian host countries to graduate from foreign direct investment that is attracted by cheap labour to higher value-added forms of investment, it is not unreasonable to assume that some investment flows will be shifted from them; in fact, some of the newly industrialized economies and other developing countries in Asia are increasingly shifting some production to their lower-wage neighbours having a reasonably educated and hard-working labour force. Because of this, though competition may be keen, least

developed countries such as Bangladesh may stand to gain from some of the future flows of such investment.

54. To position themselves for future foreign-direct-investment flows, least developed countries may find it advantageous to emphasize policies that are investment-friendly, to foster human resources development and to create a stable economic environment. In particular, developing countries that continue to attract investment have invested substantially in both physical and human capital development. Gross fixed capital formation accounted for more than 29 per cent of gross domestic product in South, East and South-East Asia (table 2). In the least developed countries, only 15 to 16 per cent of gross domestic product was invested. As to human resources development, the percentage of the population in the age group enrolled in higher or tertiary education was only 4 per cent in 1990 in low-income developing countries, 61/ compared to 16 per cent in other developing countries. This share did not change during the past two decades for low-income developing countries, while some other developing countries experienced a significant growth in enrolment. In the Republic of Korea, for example, that share increased from 16 per cent in 1970 to 39 per cent in 1990; similarly, in Chile that share went up from 13 per cent to 19 per cent during the same period. 62/ Continued investments in fixed and human capital lay the ground for improving infrastructure that would help to provide macroeconomic stability and efficiency.

55. In view of the limited private resources flowing to least developed countries, official development assistance will remain essential for providing a good part of the necessary financing for these investments. In a number of cases, structural reforms may be important for obtaining and maximizing such external financial resources. At the same time, the public support from developed-country Governments and international organizations will be essential to the success of structural adjustment by least developed countries. 63/ Without such support, it is not likely that those countries could create conditions attractive to foreign investors and generate development on a scale sufficient to attract meaningful amounts of foreign direct investment.

Notes

1/ There are 47 developing countries recognized by the United Nations as least developed countries. For a listing, see UNCTAD, The Least Developed Countries 1992 Report (United Nations publication, Sales No. E.93.II.D.3).

2/ Ibid. See also table 5 for data on per capita gross domestic product.

3/ For a detailed discussion of issues related to the liberalization of foreign-direct-investment regimes, see document E/C.10/1994/7.

4/ Data for least developed countries in Africa exclude Liberia, because this country attracts occasionally large inflows of foreign direct investment to its flags-of-convenience facility, thus distorting flows to least developed countries. Flows to least developed countries in Africa were, during these years, as follows (millions of dollars):

Foreign-direct-investment flows to Africa	1988	1989	1990
Includes Liberia	459	949	631
Excludes Liberia	168	293	355

Source: UNCTAD Programme on Transnational Corporations, based on International Monetary Fund, balance-of-payments tape, retrieved on 13 December 1993.

5/ UNCTAD Programme on Transnational Corporations, based on International Monetary Fund, balance-of-payments tape, retrieved on 13 December 1993.

6/ See UNCTAD Programme on Transnational Corporations, "Foreign direct investment in Africa: report to the Commission on Transnational Corporations" (E/C.10/1994/5).

7/ UNCTAD Programme on Transnational Corporations, World Investment Report 1993: Transnational Corporations and Integrated International Production (United Nations publication, Sales No. E.93.II.A.14), pp. 66-67.

8/ See Paul Handley, "The old and the bold: far reaching economic reforms draw mixed reviews", Far Eastern Economic Review, 4 November 1993, pp. 30-31.

9/ See UNCTAD, The Least Developed Countries 1991 Report (United Nations publication, Sales No. E.92.II.D.1), p. 13.

10/ Ibid.

11/ Ibid.

12/ For recent developments in the external financing of developing countries, see UNCTAD, Trade and Development Report, 1993 (United Nations publication, Sales No. E.93.II.D.10), pp. 49-69.

13/ The region's share of resource flows here and in other parts of this report are calculated by measuring the importance of the data on the respective region (tables 6 and 8) in the context of the table on all developing countries of the World Bank, World Debt Tables 1993-94: External Finance for Developing Countries, Volume 1, Analysis and Summary Tables (Washington, D.C., The World Bank, 1993), pp. 170-173.

14/ Ibid., p. 5.

15/ To a certain extent, the distinction between "portfolio" and "direct" investment is a definitional one and certain thresholds are established because

they are assumed to connote control. On this and the links between these two forms of investment, see "Trends in foreign direct investment", E/C.10/1994/2.

16/ "Asia's wealth", Business Week, 29 November 1993.

17/ Nihon Keizai Shimbun, 19 January 1994.

18/ The World Bank, World Debt Tables 1993-94, op. cit., table 1.8, p. 26.

19/ Despite the rapid growth of investment inflows in the Pacific islands (from an annual average of $139 million during 1981-1985 to more than $500 million in 1992), they accounted only for 2 per cent of total flows into the region in 1992.

20/ It is believed that data on investment inflows and outflows for China reported by the International Monetary Fund (like other foreign-direct-investment data) disguise some domestic investment that is re-routed through foreign affiliates in Hong Kong back into China as foreign direct investment in order to take advantage of fiscal entitlements awarded to foreign investors. See Peter Harrold and Rajiv Lall, "China: reform and development in 1992-93", World Bank Discussion Paper No. 215 (Washington, D.C., The World Bank, August 1993).

21/ Tony Walker, "Investment in China set to top $100bn", Financial Times, 8 November 1993, p. 5, and James Zhan, "The role of foreign direct investment in economic development and market-oriented reforms: the case of China", Transnational Corporations, vol. 2 (1993). Contracted foreign direct investment is expected to exceed $100 billion in 1993.

22/ Real wage increases are calculated as nominal wage increases divided by consumer prices index. Data are from International Labour Office, Yearbook of Labour Statistics, 1993 (Geneva, ILO, 1993).

23/ The World Bank, World Development Report, 1990 and 1993 (Washington D.C., 1990 and 1993), table 7, pp. 190-191 and pp. 250-251, respectively.

24/ For example, the Statute for Industrial Upgrading that came into effect in 1991 in Taiwan Province of China provides incentives to transnational corporations engaging in research and development, the enhancement of productivity, training, the establishment of international brand names and the use of environmental protection systems. See, China External Trade Development Council, Doing Business with Taiwan R.O.C. (Taipei, China External Trade Development Council, June 1991).

25/ "Lee can do", The Economist, 21 August 1993.

26/ For example, PGI (Singapore) announced its intention to set up a manufacturing plant (electric and electronic equipment) and its European research-and-development headquarters in Scotland. See, James Buxton, "First Singapore company comes to UK", Financial Times, 16 November 1993.

27/ Outflows of foreign direct investment from the newly industrialized countries to ASEAN (except Singapore) were $4.5 billion in 1992 and $2.2 billion in January-September 1993. Nihon Keizai Shimbun, 3 December 1993, p. 9.

28/ United Nations Transnational Corporations and Management Division, Transnational Corporations from Developing Countries: Impact on Their Home Countries (United Nations publication, Sales No. E.93.II.A.8).

29/ Although a $4 billion outflow was reported in 1992, it was probably inflated by the inclusion of funds that are "roundtripped" through Chinese affiliates abroad or other entities in order to be reinvested in China. See note 20.

30/ The Bank of Japan, Balance of Payments Monthly, No. 285 and 321 (Tokyo, April 1990 and April 1993). Even if foreign direct investment on an approval basis reported by the Ministry of Finance is used, the same conclusion applies. In this case, the share decreased from 59 per cent in fiscal 1989 to 30 per cent in fiscal 1992.

31/ Nihon Keizai Shimbun, 20 December 1993. The share of intraregional trade (exports) in total trade (exports) was 68 per cent for the European Union and 43 per cent for the North American Free Trade Area in 1992.

32/ UNCTAD, Ad Hoc Working Group on Investment and Financial Flows, "Case study submitted by India", TD/B/WG.1/Misc.3/Add.3, 27 May 1993, p. 28.

33/ Nihon Keizai Shimbun, 1 February 1994.

34/ A. Calderon, "Tendencias recientes de la inversión extranjera en América Latina y el Caribe: elementos de política y resultados". Paper presented at the IRELA seminar on "Foreign Direct Investment in the Third World", Segovia, Spain, 10-11 June 1993. See also the section on Latin America and the Caribbean in UNCTAD Programme on Transnational Corporations, World Investment Report 1993: Transnational Corporations and Integrated International Production, pp. 50-54.

35/ Ibid., p. 45.

36/ See J. Ramos, "Crecimiento, crisis y viraje estratégico", CEPAL Review, No. 50 (August 1993), pp. 65-73.

37/ Economic Commission for Latin America and the Caribbean, Estudio Económico de América Latina y el Caribe 1992 (Santiago, ECLAC, 1992).

38/ Michael Mortimore, "The conduct of Latin America's creditor banks", CEPAL Review, No. 37 (April 1989), pp. 7-26; and UNCTC, Transnational Banks and the International Debt Crisis (United Nations publication, Sales No. E.90.II.A.19).

39/ Access to American Depository Receipts by Latin American countries began with a Chilean telephone company in July 1990 and was given a big boost by the $1.9 billion offering of shares by a Mexican telephone company in May 1991. This instrument consists of the issue of negotiable certificates by United

States banks ("depository banks") in representation of foreign shares. This mechanism facilitates intermediated share issues in the United States which are freely tradable, quoted in dollars and with dividends paid in dollars. The authorization of the Securities and Exchange Commission is required. Another related mechanism - Global Depository Receipts - allows for certificates to be floated simultaneously in different world stock markets.

40/ This mechanism allows foreigners to purchase shares on the local stock market in an indirect fashion via a controlled fund measured in dollars and quoted in global stock markets.

41/ "A survey of Third World finance: new ways to grow", The Economist, 25 September 1993.

42/ G. Calvo, L. Leiderman and C. Reinhart, "Capital inflows and real exchange rate appreciation in Latin America: the role of the external sector", IMF Staff Papers, vol. 40 (March 1993), pp. 108-151.

43/ None the less, it should be noted that Latin America has accounted for about two thirds of the 1,100 privatizations that took place during 1988-1992, as measured by revenue and foreign exchange receipts. See Frank Sader, "Privatization and foreign investment in the developing world, 1988-92", The World Bank Working Papers (Washington, D.C., The World Bank, October 1993).

44/ "A survey of Latin America: under construction", The Economist, 13 November 1993, p. 22. A caveat needs to be added here, however. In the case of Mexico, overall output growth since the reform process started in 1985 has barely exceeded the rate of growth of population. And the Chilean economy is still vulnerable to external shocks, because of strong dependence on the prices of copper, fish meal, pulp and paper, and fruit and on rather volatile and unpredictable capital flows.

45/ B. Kosacoff and G. Bezchinsky, De la Sustitución de Importaciones a la Globalización (Buenos Aires, ECLAC, May 1993); and J. M. Fanelli and J. L. Machinea, "Capital movements in Argentina". Paper presented to the ECLAC/IDRC Seminar on "New Private Flows to Latin America", Santiago, Chile, 6-7 December 1993. If the proceeds from debt-equity swaps are being used to reduce debt, this can free up savings for investment purposes.

46/ See AméricaEconomia, special issues, December 1992 and December 1993.

47/ See UNCTAD Programme on Transnational Corporations, World Investment Directory 1993, volume IV, Latin America and the Caribbean (United Nations publication, forthcoming).

48/ SECOFI, "La inversión extranjera en Mexico", Comercio Exterior, 43 (March 1993), p. 213. Also see Edgar Ortiz, "TLC e inversión extranjera en México", Comercio Exterior, 43 (October 1993), pp. 971-972.

49/ In 1992 alone, $440 million (or 56 per cent) of the foreign direct investment that entered the country that year went into petroleum, according to National Planning Department figures; see "Colombia: opening the door to foreign investment", a special sponsored section in Institutional Investor, 18

(December 1993), p. 4. Also see "Fin de siesta", AméricaEconomia, 79 (December 1993), p. 40.

50/ Michael Mortimore, "Transforming sitting ducks into flying geese: the example of the Mexican automobile industry", forthcoming; Mauricio de María y Campos, "Reestructuración y desarrollo de la industria automotriz Mexicana en los años ochenta: evolución y perspectivas", Estudios e Informes de la CEPAL, 83 (August 1992); and UNCTC, Foreign Direct Investment and Industrial Restructuring in Mexico, UNCTC Current Studies, Series A, No. 18 (United Nations publication, Sales No. E.92.II.A.9).

51/ The following investments were announced by automobile producers in Brazil and Argentina as of the end of 1993: Ford $1,600 million, General Motors $1,500 million, Fiat $755 million and Kia $500 million; see AméricaEconomia, Special Number, 1993-1994, pp. 23-24.

52/ See UNCTAD Programme on Transnational Corporations, World Investment Directory 1993, volume IV, Latin America and the Caribbean.

53/ M. R. Agosin and R. Ffrench-Davis, "La liberalización comercial en América Latina", CEPAL Review, 50 (August 1993), p. 44; and Asad Alam and Sarath Rajapatirana, "La reforma comercial en América Latina y el Caribe", Finanzas y Desarrollo (September 1993), p. 45.

54/ ECLAC, El regionalismo abierto en América Latina y el Caribe (Santiago, ECLAC, 1994), p. 10.

55/ It should also be mentioned that a number of small economies in the region, mostly in the Caribbean, are linked to the European Union through the Lomé Convention. However, this arrangement is not a free trade agreement, although it provides access to the European Union market on a preferential basis and contains a number of provisions aimed at stimulating foreign direct investment. It might be further mentioned in passing that a noteworthy extraregional forum - the Asia and Pacific Economic Cooperation Organization - admitted Mexico as a member in 1993, and Chile is expected to be admitted in 1994. While this obviously does not carry as much importance as a free trade agreement with extraregional partners, it does underline the growing international orientation of countries such as Mexico and Chile.

56/ See UNCTAD Programme on Transnational Corporations, World Investment Report 1993, op. cit., pp. 50-54.

57/ It might be recalled that, in the context of the clustering of international trade and investment, Brazil was one of only two Latin American countries clearly located in a non-North American cluster; the other country was Peru. See UNCTC, World Investment Report 1991: The Triad in Foreign Direct Investment (United Nations publication, Sales No. E.91.II.A.12), p. 56.

58/ See UNCTAD Programme on Transnational Corporations, World Investment Report 1993, op cit., and World Investment Report 1992, op. cit., pp. 40-44.

59/ See UNCTC, Regional Economic Integration and Transnational Corporations in the 1990s: Europe 1992, North America and Developing Countries, UNCTC Current Studies, Series A, No. 15 (United Nations publication, Sales No. E.90.II.A.14).

60/ UNCTAD Programme on Transnational Corporations, Explaining and Forecasting Regional Flows of Foreign Direct Investment (United Nations publication, Sales No. E.94.II.A.5), pp. 25-28.

61/ According to the definition of the World Bank that uses $635 gross national product per capita as cut-off criterion, there were 40 low-income developing countries in 1991.

62/ The World Bank, World Development Report 1993: Investing in Health (Washington, D.C., The World Bank, 1993), table 29, pp. 294-295.

63/ As regards the latter, examples are the Structural Adjustment Facility (SAF) and the Enhanced Structural Adjustment Facility (ESAF) established in 1986 and 1987, respectively, in the International Monetary Fund. Low-income developing countries can obtain concessional loans up to 50 per cent of the country's IMF quota under the SAF and 110 per cent under the ESAF. As of July 1993, there were 36 low-income developing countries eligible under the SAF and 29 countries eligible under ESAF. See Susan Schadler, Frank Rozwadowski, Siddharth Tiwari and David O. Robinson, Economic Adjustment in Low-Income countries: Experience under the Enhanced Structural Adjustment Facility, IMF Occasional Paper 106 (Washington, D.C., IMF, 1993). The Special Programme of Assistance (SPA) for sub-Saharan Africa in the World Bank was launched in 1990. Currently 27 countries are eligible for this programme.